Swiss Federal Council initiates the consultation phase for Corporate Tax Reform III

Executive summary

On 22 September 2014, the consultation phase for the third Swiss Corporate Tax Reform (CTR III) was initiated and the Swiss Finance Minister Eveline Widmer-Schlumpf presented the technical details during a press conference held the same day. During the next four months, political parties, cantons and interested associations are invited to share their views on the proposed measures to strengthen Switzerland’s attractiveness as a business location.

With the much anticipated legislative draft, the Swiss Government once again reaffirmed its intention to foster the fiscal attractiveness of Switzerland. The proposed measures should ensure that Switzerland will have a sustainable, internationally accepted and competitive tax system for multinational companies.

Since 2005, Switzerland’s preferential cantonal tax regimes have been under increasing international pressure. The proposed corporate tax reform has become necessary given the accelerated review of international tax practices by the European Union (EU) and the Organisation for Economic Cooperation and Development (OECD). The final report on measures to strengthen Switzerland’s tax competitiveness issued in December 2013 already outlined the strategic direction of the upcoming tax reform. The draft legislation and the explanatory report finally confirm that the cantonal taxation regimes for holding, domiciliary and mixed companies shall be abolished in the next four to six years and be replaced by new competitive regimes which are in line with international taxation standards. Furthermore, the Swiss Government also made clear that the practice of international profit allocation of principal companies and the treatment of Swiss finance branches for tax purposes are no longer sustainable solutions, considering the recent and ongoing changes in international tax policy regulations (e.g., OECD Base Erosion and Profit Shifting (BEPS), the EU Code of Conduct for business taxation and EU state aid rules).
Detailed discussion

Proposed measures

The Federal Council is proposing to abolish the existing tax regimes that are no longer internationally accepted. In order to remain competitive from a fiscal standpoint, the Federal Council suggests introducing the following measures:

Introduction of internationally accepted rules

License box

Although international developments regarding the acceptance of license box regimes are still in flux and the final solutions difficult to anticipate, Switzerland plans to introduce a license box on the cantonal/communal level in order to promote the development and the use of intellectual property (IP) by Swiss companies. The contemplated license box shall be similar to the UK patent box. Accordingly, income derived from patents, supplementary protection certificates, exclusive licenses for patents and so-called first-notifier protection in accordance with Article 12 of the Swiss Law on Therapeutic Products will qualify for the box, whereas trademarks cannot benefit. The Swiss license box shall offer a privileged treatment of “embedded IP” income by using a top-down approach (so-called residual method) for the calculation of the qualifying IP income.

The maximum tax base reduction on the cantonal/communal level shall amount to 80%. Consequently, qualifying IP income would be subject to an effective tax rate of around 10% including the federal tax.

Considering that both the EU and the OECD are currently reviewing all existing IP box regimes, the Swiss license box regime may be amended during the legislative process in order to comply with the latest international standards.

Notional interest deduction on equity (NID)

The proposed NID shall ensure equal tax treatment of equity and debt since financing decisions shall not be impacted by fiscal considerations. This view is also shared by the EU and the OECD. Hence, the introduction of an NID concept is considered an internationally accepted regime. The NID shall be introduced both on the federal and cantonal/communal level and shall be limited to the “surplus equity,” which refers to the part of equity that exceeds an average, sound equity financing of a company.

The applicable interest rate shall be based on the yield of 10-year government bonds plus 50 basis points. Additionally, the Federal Council suggests a minimum interest rate of 2%. The details of the calculation of the risk weighted assets will most likely be determined in a circular letter.

Cantonal tax rate reduction

The cantons may reduce their ordinary tax rates in order to enhance their attractiveness. In addition, the cantons shall be entitled to reduce the capital tax on net equity related to participations, IP or group-loans.

Other measures

Step-up

In case of a change of the tax status, the proposed legislation allows for a tax-neutral step-up of the built-in gains as well as (self-generated) goodwill created during the privileged taxation period followed by a tax effective amortization over the following 10 years.

Change of the Swiss participation exemption regime

It is proposed to replace the current indirect exemption with a direct exemption model. This means that any income or loss deriving from participations shall no longer be tax effective.

Tax loss carry forward

Tax loss carry forward shall be deductible for an unlimited period of time while based on the current law tax losses expire after seven years. However, the loss offsetting shall be limited to 80% of the taxable profit (before use of tax losses). Furthermore, it is suggested to adopt a “Marks & Spencer” regime for final tax losses incurred by Swiss and foreign subsidiaries whereby tax losses could be utilized by the Swiss parent company to offset taxable income.

In addition, it is contemplated to abolish the 1% one-time capital duty on capital contributions.

Financing

CTR III may lead to a significant reduction of tax revenue. Therefore, it is suggested to introduce a capital gains tax on securities and to
amend the partial taxation system for dividend income for private individuals.

**Timing for new tax law**

Interested parties can provide their comments until 31 January 2015. Aside from the feedback received in response to the consultation, the Federal Council will also take into account international developments that occur in the meantime. The Federal Council’s dispatch for the attention of the Parliament is expected in the first semester 2015 so that the draft bill can be considered by the First Chamber during the winter session 2015. The parliamentary discussions may then be finished in the middle of 2016 at the earliest. In this case and if no referendum is taken, the new law may enter into force between 2018 and 2020.

**Current tax law**

Given the fact that the new law will not enter into force until 2018-2020, the current tax regimes will remain valid for the next four to six years.

**Webcast**

On 2 October 2014, EY Switzerland will host two webcasts (in German and English) on the CTR III. These webcasts will further analyze the implications resulting from the proposed measures. In addition, the webcast panel will discuss reactions to the draft legislation and provide additional details about the new regimes. To register for the webcast, please contact diana.wittig@ch.ey.com.

---

**Endnotes**


2. For background see *C-446/03, Marks & Spencer*. 
For additional information with respect to this Alert, please contact the following:

**Ernst & Young AG, Zurich**
- Daniel Gentsch  +41 58 286 36 13  daniel.gentsch@ch.ey.com
- Rainer Hausmann  +41 58 286 31 93  rainer.hausmann@ch.ey.com
- Peter Bruelisauer  +41 58 286 44 43  peter.bruelisauer@ch.ey.com
- Marco Mühlemann  +41 58 286 31 28  marco.muehlemann@ch.ey.com

**Ernst & Young AG, Zug**
- Kersten A. Honold  +41 58 286 31 66  kersten.honold@ch.ey.com

**Ernst & Young SA, Geneva**
- Markus Frank Huber  +41 58 286 31 89  markus-frank.huber@ch.ey.com
- Karen Simonin  +41 58 286 56 53  karen.simonin@ch.ey.com

**Ernst & Young LLP, Swiss Tax Desk, New York**
- Thomas Semadeni  +1 212 773 84 42  thomas.semadeni@ey.com
- Antonio Pérez  +1 212 773 53 50  antonio.perez@ey.com
About EY

EY is a global leader in assurance, tax, transaction and advisory services. The insights and quality services we deliver help build trust and confidence in the capital markets and in economies the world over. We develop outstanding leaders who team to deliver on our promises to all of our stakeholders. In so doing, we play a critical role in building a better working world for our people, for our clients and for our communities.

EY refers to the global organization, and may refer to one or more, of the member firms of Ernst & Young Global Limited, each of which is a separate legal entity. Ernst & Young Global Limited, a UK company limited by guarantee, does not provide services to clients. For more information about our organization, please visit ey.com.

© 2014 EYGM Limited.
All Rights Reserved.

EYG No. CM4753

This material has been prepared for general informational purposes only and is not intended to be relied upon as accounting, tax, or other professional advice. Please refer to your advisors for specific advice.

ey.com